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RUEHBY/AMEMBASSY CANBERRA 1282
RUEHBJ/AMEMBASSY BEIJING 1898
RUEHKA/AMEMBASSY DHAKA 4895
RUEHNE/AMEMBASSY NEW DELHI 4818
RUEHUL/AMEMBASSY SEOUL 8370
RUEHKO/AMEMBASSY TOKYO 5932
RUEHCN/AMCONSUL CHENGDU 1489
RUEHCHI/AMCONSUL CHIANG MAI 1653
RUEHCI/AMCONSUL KOLKATA 0347
RUEAIIA/CIA WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RUEKJCS/DIA WASHDC
RUEHGV/USMISSION GENEVA 3819
RHEHNSC/NSC WASHDC
RUEKJCS/SECDEF WASHDC
RUEKJCS/JOINT STAFF WASHDC
RUCNDT/USMISSION USUN NEW YORK 1757
RUEHBS/USEU BRUSSELS

C O N F I D E N T I A L SECTION 01 OF 03 RANGOON 000490

SIPDIS

STATE FOR EAP/MLS; INR/EAP; OES FOR JMOTKE AND ACOVINGTON;
EAP FOR JYAMAMOTO; EEB FOR TSAEGER
PACOM FOR FPA;
TREASURY FOR OASIA: SCHUN

E.O. 12958: DECL: 06/17/2018
TAGS: [ECON](#) [ENRG](#) [PGOV](#) [EPET](#) [BM](#)
SUBJECT: BURMA: DAEWOO AND CNPC TO JOINTLY DEVELOP GAS
FIELDS

REF: A. RANGOON 253
[1](#)B. RANGOON 156
[1](#)C. RANGOON 003

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Classified By: Economic Officer Samantha A. Carl-Yoder for Reasons 1.4
(b and d)

[1](#)1. (C) Summary. Officials from Daewoo International Corp. and China National Petroleum Corporation (CNPC) on May 29 signed a Memorandum of Understanding (MOU), calling for future cooperation on oil and gas exploration in Burma. Daewoo Drilling Manager Bruce Leach confirmed that the two companies will conduct joint exploratory drilling in Daewoo's deep sea block AD-7, adjacent to the Shwe Gas fields, in late [1](#)2008. According to Daewoo Business Development Director Jong Bin Choi, the MOU is a win-win for both companies: Daewoo can minimize its financial risk by partnering up with CNPC for costly exploratory drilling in AD-7 while CNPC looks to secure the future delivery of additional gas reserves. Daewoo continues to negotiate with CNPC subsidiary PetroChina on the sale of Shwe Gas. Although Daewoo officials predicted a final sales contract by August 2008, Choi admitted that negotiations were not progressing as quickly as anticipated. Daewoo officials hope to ink a final contract by the end of [1](#)2008. The company continues to conduct exploratory drilling in the A-1 and A-3 blocks. The discovery of additional proven reserves may be the impetus for Daewoo to reconsider constructing an LNG terminal, should the sale of Shwe Gas to China fall through. End Summary.

A Win-Win Situation

¶2. (C) Daewoo International Corporation, operator of the A-1 and A-3 Shwe Gas fields, was cultivating a strong business relationship with Chinese oil and gas companies, Daewoo Business Development Director Jong Bin Choi told us. For the past year, Daewoo has quietly looked for partners to assist with the development of its deep sea block AD-7, located adjacent to the Shwe Gas fields. A partnership with China National Petroleum Corporation (CNPC) made sense, Choi explained, since CNPC controlled the rights to develop the other three deep sea blocks surrounding the Shwe Gas fields, AD-1, AD-6, and AD-8. On May 29, officials from Daewoo and CNPC signed a Memorandum of Understanding (MOU), which called for future collaboration on oil and gas exploration in Burma.

While several high-level Daewoo officials told us that the MOU was nothing more than a declaration of a general partnership between the two companies, Choi admitted that the MOU was the first step toward a partnership to develop the blocks surrounding the Shwe fields. According to Daewoo Drilling Manager Bruce Leach, Daewoo and CNPC will jointly construct one exploratory well in Daewoo's AD-7 block in late ¶2008.

¶3. (C) The partnership with CNPC will greatly benefit Daewoo, Choi declared. A partnership with CNPC allows Daewoo to move forward with its plans to develop Burma's oil and gas sector while reducing the company's overall financial risk. One exploratory well in deep water can cost up to \$80 million, Leach commented. Cost-sharing with CNPC allows Daewoo to drill twice as many exploratory wells on the same budget. Additionally, Daewoo, which has little experience in deep sea drilling, can benefit from CNPC's expertise in this area. Daewoo officials also expect that enhanced cooperation on oil and gas development will enable the company to

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increase its trade dealings with China, particularly its sales of steel and machinery. The MOU is not just an energy contract, Choi stated, but offers a way for Daewoo to expand its profitability on all fronts.

¶4. (C) The Chinese remain desperate for natural gas. In partnering with Daewoo to explore the deep sea blocks surrounding the Shwe Gas fields, CNPC and its subsidiary, PetroChina, expect that any discoveries of gas would be added to the Shwe Gas reserves and thus sold to China, Leach commented. Choi acknowledged that CNPC would be interested in acquiring shares in Daewoo's AD-7 block if the exploratory drilling yields proven gas reserves. Currently, there is no plan for joint exploration of CNPC's deep sea blocks AD-1, AD-6, or AD-8, although Leach intimated that the two companies could discuss this possibility in 2009.

Still No News on Shwe Sales

¶5. (C) Daewoo and PetroChina have yet to sign the final contract for the sale of Shwe Gas, despite more than 18 months of negotiations and continued pressure from the Government of Burma (Refs A and B). According to Daewoo Principal Process Engineer Andrew Hay, the two companies have yet to agree on the price of gas. Since there is no international benchmark price for gas (as there is with oil), companies must agree on a long term price per gas unit (one unit is the equivalent of one million British Thermal Units - MMBtu), which usually reflects the market price in the region where the gas is sold. PetroChina does not want to pay the Asian price for gas, currently at \$10 per MMBtu. Instead it wants to import large quantities of gas for less than the market value to offset the high cost - estimated at more than \$2 billion - of the 900-mile pipeline from Kunming to the Bay of Bengal. Purchasing Shwe Gas and transporting it to Western China is not economically viable for PetroChina, Choi admitted. However, China needs natural gas, particularly in the Western region, so Daewoo remains confident that PetroChina will eventually agree to its price. The company expects to conclude the final sales contract by the end of

2008, a delay of more than eight months (Ref B).

¶6. (C) Continued delays in the sales contract further pushes back the date of production, Leach told us. Daewoo needs at least three years to develop the Shwe Gas fields, design and construct the well heads, and build a pipeline to the PetroChina pipeline on Ramri Island. PetroChina will need at least three years, more likely four, to construct the pipeline, Leach commented. The earliest Daewoo can produce the natural gas to send to China is late 2012. Final delivery of gas will depend on whether PetroChina can build a pipeline in the allotted time. Leach doubted that the Chinese could build the 900-mile pipeline by 2012.

¶7. (C) When asked about whether the GOB still demanded that Daewoo pay additional taxes on the profits from Shwe Gas sales (Ref A), Hay informed us that the Ministry of Energy had not raised the issue since April. However, Daewoo officials expect that the GOB will again raise the issue as Daewoo and PetroChina move closer to a final agreement. Hay emphasized that Daewoo officials will not sign the final sales contract with PetroChina until the matter was resolved, thereby delaying the GOB's income from the sale of Shwe Gas.

Keeping its Options Open

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¶8. (C) Choi acknowledged that negotiations with PetroChina were not going as well as expected, and that Daewoo was "keeping its options open." Daewoo continued to conduct exploratory drilling in the A1 and A3 blocks; if more proven reserves are found, Daewoo would have enough gas reserves to justify the construction of a liquefied natural gas (LNG) terminal. Choi commented that it was easier, cheaper, and more cost efficient to ship LNG than natural gas through a pipeline. Demand for LNG remains high worldwide and several companies, including Korean Gas Company, have approached Daewoo about its future plans for LNG. Choi emphasized, however, that Daewoo was committed to selling Shwe Gas to PetroChina, assuming the price was right.

Comment

¶9. (C) Daewoo International Corp., which has invested over \$100 million in the development of the Shwe Gas fields, has allied itself with CNPC and PetroChina as a way to ensure profitability. Although Daewoo would prefer to sell LNG rather than natural gas, the reality is that the Shwe Gas fields lack sufficient proven reserves to supply an LNG terminal. Additionally, the GOB continues to push Daewoo to finalize the contract with PetroChina; in order for Daewoo to ensure its continued involvement in the development of Burma's oil and gas sector, it will sell Shwe Gas to the Chinese. Daewoo may be a newcomer to the oil and gas sector, but by aligning itself with the Chinese, it expects to profit over time. PetroChina may think it is playing hardball over the price of gas, but the longer it delays the final contract, the higher the market price of natural gas - in the end, Daewoo will collect its profits and China will receive its natural gas.

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